

THE JAPAN-GEORGIA BILATERAL INVESTMENT TREATY

Introduction

On 29 January 2021, Japan and Georgia signed a bilateral investment treaty titled the Agreement between Japan and Georgia for the Liberalisation, Promotion and Protection of Investment (**Japan-Georgia BIT** or **BIT**). This is the first BIT signed by either Japan or Georgia since the outbreak of the COVID-19 pandemic. It is expected that the BIT will enter into force later this year once it has been through the requisite ratification procedures in Japan and Georgia.

Upon signing the BIT, Georgia's Minister of Economy was reported to have said *"We will do our best to bring as many Japanese investors as possible into various fields of the Georgian economy to create new jobs especially in the post-Covid period, when we need active investments"*. This builds upon a steady increase of Japanese investment into Georgia particularly in the energy sector. For example, last year a major Japanese utility company acquired a significant stake in a Georgian hydropower company.

The Japan-Georgia BIT contains wide-ranging investment protections for investors from Georgia and Japan. This briefing provides further detail on who is covered and how these rights may be used. In summary, consistent with its own aims, and the emerging Japanese 'standard form' for investment treaties, the Japan-Georgia BIT is favourable from an investor's perspective. Importantly, the treaty has "teeth" in the form of an investor-State dispute settlement (**ISDS**) mechanism.

As well as looking at the provisions of the treaty in more detail in this briefing, we highlight some of its limitations and exclusions, for example, for measures aimed at protecting public health. There are also other exclusions specifically focused on the construction, engineering, electricity, gas and oil sectors.

New protections for Japanese and Georgian investors

Who and what is covered?

The Japan-Georgia BIT protects "*investors*" from Japan and Georgia. The definition of "*investor*" includes Japanese and Georgian nationals as well as "*enterprises*". An "*enterprise*" is defined broadly to cover most forms of company, organisation, trust, partnership or other legal form of association that is "*duly constituted or organised under the applicable laws and regulations*". However, as is commonly the case in investment treaties of this kind, there is a 'Denial of Benefits' clause which excludes Japanese or Georgian enterprises taking advantage of rights conferred by the treaty if such enterprises are subject to the majority ownership or control of a foreign third party that does not have "*substantial business activities*" in Japan or Georgia (as applicable). Whether or

Key Takeaways

Wide-ranging investment protections under the Japan-Georgia Investment Treaty:

- Signed 29 January 2021
- The treaty contains robust protections for Japanese investors in Georgia and Georgian investors in Japan
- The protections are subject to various limitations and exclusions
- Investment protection is backed-up by ISDS
- Japan is continuing to expand its investment treaty programme notwithstanding the COVID-19 pandemic
- Georgia is also continuing to expand its treaty programme notwithstanding Georgia's experience of being a respondent state in investor-state arbitration

not the person or enterprise from the third-party state has "*substantial business activities*" is a matter that has been the subject of dispute before international tribunals. Factors that may be taken into consideration in determining whether the requirement has been satisfied include whether the relevant entity has a physical office or pays tax in the home state.

An "*investment*" protected under the Japan-Georgia BIT is also defined widely and includes property rights, shares, stocks, bonds, debentures, intellectual property rights, licences, rights under contracts and other assets. However, in order to qualify for protection under the BIT, investments must have been made "*in accordance with the applicable laws and regulations*" of Japan or Georgia. Investments must also have the "*characteristics*" of an investment which include the commitment of capital, expectation of profit or assumption of risk. Case law on what, as a matter of fact, constitute these characteristics is unsettled but generally investments will be covered if the investor can establish that the investment was not highly speculative nor in the nature of a one-off, short-term transaction.

It should also be noted that investment protections created by the Japan-Georgia BIT will apply to investments made prior to the entry into force of the BIT. However, claims or disputes in relation to events which occurred prior to such entry into force will *not* be actionable under the BIT.

To maximise an investor's ability to rely on the treaty, investors should seek legal advice to ensure that their investment complies with host state laws and that steps have been taken to demonstrate that the investment is otherwise compliant with the requirements of the BIT. Failure to do so may, in a dispute situation, increase the risk of successful jurisdictional objections by the host state on the basis that the investment is not covered because of a legal deficiency or because it does not have the "*characteristics*" of an investment.

What protections are available?

Amongst other rights, the Japan-Georgia BIT includes the following key protections for covered foreign investors and investments:

National treatment (Article 2): this prohibits discrimination based on an investor's nationality. In other words, Japanese investors in Georgia are entitled to the same treatment that Georgia grants to local investors.

Protection from expropriation and nationalisation (Article 11): Japan and Georgia may not unlawfully expropriate or nationalise investments covered by the Japan-Georgia BIT except for a public purpose, in accordance with due process on a non-discriminatory basis and accompanied by payment to the investor by the state of "*prompt, adequate and effective*" compensation.

Fair and equitable treatment (FET) (Article 4): Japanese and Georgian investments must be treated in a fair and equitable manner by the host State. This protects against discriminatory or arbitrary treatment and governmental measures that violate the investor's legitimate expectations. However, the FET standard in this treaty is limited to the "*customary international law*" standard, which arguably offers a lower standard of protection than other types of FET clauses found in investment protection treaties (although Japan typically qualifies its FET clauses in this manner).

Full protection and security (FPS) (Article 4): the governments of Japan and Georgia must provide physical protection (e.g. police or military protection) to covered investments, which must be at least the same as the protections

provided to host State nationals. Notably, this protection is also linked to the "*customary international law*" standard. However, it is also bolstered by provisions concerning 'Protection from Strife' (Article 12) which seek to ensure equality for covered investors in entitlement to compensation made as a result of losses caused by civil war, revolution or other kind of violent disruption.

Prohibition of performance requirements (Article 6): this Article prohibits the imposition by Japan or Georgia on covered investors of conditions on the management or operation of covered investments such as import/export quotas or requirements to use locally produced goods or materials.

Free transfers (Article 14): subject to certain limitations, covered Japanese and Georgian investors are entitled to free transfer of capital, profits, interests, royalties, fees, dividends, or other cashflows related to their investments.

Most-favoured nation treatment (MFN) (Article 3): Japanese and Georgian investors covered by the BIT are entitled to be treated no less favourably than other foreign investors active in the host State. As is typical in Japan's investment treaties, this protection is limited to investors "*in like circumstances*" when compared to third party investors granted rights under other treaties. It also expressly excludes application to procedural rights (i.e. ISDS).

Limitations and Exclusions

Although the protections for investors provided by the Japan-Georgia BIT are wide-ranging, there are various limitations and exclusions of which investors or potential investors should be aware. In particular, we note that measures which are designed and applied to protect "*legitimate public welfare objectives, such as public health, safety and the environment*" will not constitute expropriation under Article 12 except "*in rare circumstances*"¹. These types of provisions are becoming more frequent in investment treaties and are likely to become even more common in light of the pressures on host states to take measures to prevent the spread of COVID-19 which, at the same time, have had detrimental effects on business, including on foreign investments. As a general principle, to benefit from the exclusion, governments will still have to show that the measures taken were enacted in good faith and not made in violation of their own laws and processes. Some tribunals may also apply a proportionality test to the measures.

Other obligations are limited by reservations including in the Annex which excludes from certain protections existing measures that do not conform with the treaty (e.g. the Japanese Mining Law requirement that only a Japanese national or legal person may hold mining rights in Japan will not be considered a violation of the 'National Treatment' protection). There are further reservations in respect of future measures applied to particular industry sectors. We note in particular the exception in the Schedule of Georgia which allows Georgia to "*adopt or maintain any measure relating to investment in construction and related engineering activities that not less than 50 percent of the entire staff must be citizens of Georgia*". Georgia's Schedule also limits the application of Article 2 (National Treatment) and Article 6 (Prohibition on Performance Requirements) to measures which may affect Japanese investments in the electricity, gas and oil sectors.

¹ Similar wording was used by Japan prior to the pandemic in some of its more recent investment treaties, for example, with Argentina (2018) and Morocco (2020).

It is important for Japanese and Georgian investors expecting to rely on the protections in the Japan-Georgia BIT to be aware of any potential exclusions and to consider carefully whether their investments might be better protected through alternate structures (which allow potential recourse under other international agreements).

Enforceable rights and obligations

The Japan-Georgia BIT contains an ISDS mechanism (Article 22) which allows investors to enforce rights granted under the treaty through international arbitration. Specifically, under Article 22, Japan and Georgia consent to the submission of an investment dispute for arbitration either under the rules of the International Center for the Settlement of Investment Disputes (**ICSID**) or the Rules of the United Nations Commission on International Trade Law (**UNCITRAL Rules**). Both Japan and Georgia are members of the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (**New York Convention**) and the Convention on the Settlement of Investment Disputes between States and Nationals of other States (**ICSID Convention**). This means an arbitral award made in favour of a covered investor can be enforced against the relevant state (Japan or Georgia) in the territory of any member of the relevant convention.

This ISDS clause is similar to the majority of investment treaties entered into by Japan in recent years and provides Japanese and Georgian investors with access to a dispute settlement process conducted outside the jurisdiction of either party. The availability of this protection mitigates against the political risk associated with investments into Georgia from Japan, which may in turn reduce the cost of capital for Japanese investors.

Georgia was first sued under an investment treaty in 2005 in the case of *Kardassopoulos v Georgia*. In this case Mr Kardassopoulos, a Greek investor in the oil sector, was awarded USD15 million in compensation pursuant to a finding by the Tribunal that Georgia had unlawfully expropriated Mr Kardassopoulos' rights under an oil concession. Georgia has since been a respondent party to a further 13 claims brought by investors under international treaties. A number of these claims are still pending and in total four claims brought by investors against Georgia have been successful with other claims being settled commercially or discontinued. It is notable therefore that Georgia continues to see agreement to treaties containing ISDS as an important provision for attracting foreign investment.

By contrast, Japan has never been a respondent state under an investment treaty. However, Japanese investors are increasingly prepared to use investment treaties as a means of gaining leverage in negotiations with foreign governments as well as to protect their rights through commencement of investor-state arbitration proceedings.

Further Information

Extensive guidance on investment treaty structuring and resolving disputes with foreign governments is available from Clifford Chance. This note is an overview only and is not legal advice. For further explanation on the protections available under the Japan-Georgia BIT, or if you would like to know more about using investment treaties to protect your international investments more generally, please contact one of the individuals listed below. Please also see our further [information on investment treaty planning](#) and the [Japan-ASEAN investment treaty](#).

CONTACTS



Peter Harris
Counsel, Tokyo

T +81 3 6632 6635
E peter.harris
@cliffordchance.com



Sam Luttrell
Partner, Perth

T +61 8 9262 5564
E sam.luttrell
@cliffordchance.com



Romesh Weeramantry
Counsel, Singapore

T +65 6410 2257
E romesh.weeramantry
@cliffordchance.com



Yusuke Abe
Partner, Tokyo

T +81 3 6632 6332
E yusuke.abbe
@cliffordchance.com



Hans Menski
Partner, Tokyo

T +81 3 6632 6669
E hans.menski
@cliffordchance.com



Natsuko Sugihara
Partner, Tokyo

T +81 3 6632 6681
E natsuko.sugihara
@cliffordchance.com

This publication does not necessarily deal with every important topic or cover every aspect of the topics with which it deals. It is not designed to provide legal or other advice.

www.cliffordchance.com

Clifford Chance (Gaikokuho Kyodo Jigyo)

Palace Building, 3rd floor

1-1, Marunouchi 1-chome, Chiyoda-ku, Tokyo
100-0005, Japan

© Clifford Chance 2021

Abu Dhabi • Amsterdam • Barcelona • Beijing •
Brussels • Bucharest • Casablanca • Dubai •
Düsseldorf • Frankfurt • Hong Kong • Istanbul •
London • Luxembourg • Madrid • Milan •
Moscow • Munich • Newcastle • New York •
Paris • Perth • Prague • Rome • São Paulo •
Seoul • Shanghai • Singapore • Sydney •
Tokyo • Warsaw • Washington, D.C.

Clifford Chance has a co-operation agreement
with Abuhimed Alsheikh Alhagbani Law Firm
in Riyadh.

Clifford Chance has a best friends relationship
with Redcliffe Partners in Ukraine.